



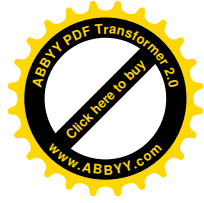
ISBN: 1646-8929

IET Working Papers Series
No. **WPS06/2008**

Monika Urbanowicz
(e-mail: monika.urbanowicz@wp.pl)

Concept of Customer Relationship Management as an example of innovation in banking sector

Grupo de Inv. "Innovation Systems"
IET
Research Centre on Enterprise and Work Innovation
Centro de Investigação em Inovação Empresarial e do Trabalho
Faculdade de Ciências e Tecnologia
Universidade Nova de Lisboa
Monte de Caparica
Portugal



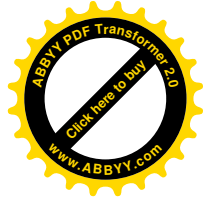
□ *Everybody talks about financial innovation,
but (almost) nobody empirically
tests hypotheses about it.* □

Frame and White

Concept of Customer Relationship Management as an example of innovation in banking sector

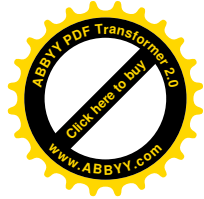
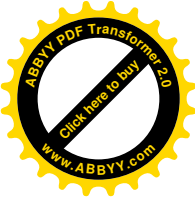
Author: Monika Urbanowicz

Lisboa 18.05.2008



Index

| | |
|--|-----------|
| 1 Innovations in banking sector | 3 |
| 2 Concept of Customer Relationship Management | 5 |
| 3 Benefits of introduction CRM systems | 7 |
| 4 Technology in banking | 9 |
| 5 Relations with customers in banking industry | 11 |
| 6 Customer Relationship Management as an innovation | 16 |
| 7 Bibliography | 18 |

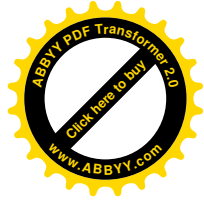


1 Innovations in banking sector

The origin of word *innovation* comes from Latin word "innovatus" and means renewal or renewed. The dictionary definition of the concept of innovation is the introduction of something new, a newly introduced new, reform. However nowadays very often innovation is understood only as a new product, whereas the meaning of this concept is much wider – it could be a new service, new process, new idea or technology. Financial Innovation could be understood as something new which is supposed to reduce costs, risk, or provide improved product, service, that better meets needs of demand of financial market's participants demand. The objective of financial market innovation can be diverse, for example making the financial service offered on the market cheaper to use, more available or of higher quality. In financial innovation we can distinguish four following groups:

- Product innovations – offering of non existing previously products
- Services innovations – new methods or distribution channels
- Process innovations – new type of production processes
- Organization – new forms of organizations

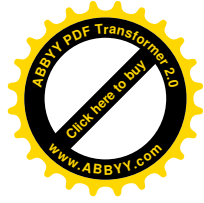
In financial sector main entities participating in creation, implementation and taking advantage of innovation are financial institutions, customers, regulation institutions, technology suppliers, society as a whole, and also entities from the bank itself such as owners, workers and managers. We can distinguish two groups of factors which create the need for innovation. In the first, according with the principle of rationality behaviour of entrepreneurs and consumers, we assume that they will tend to look for improved products, processes and organizational structures. In this context investment in research and development should bring effects in the form of more efficient allocation of capital or greater income from in financial transactions. The second group of factors for creating the need for innovation constitute the uncertainty of future environment, its fluctuations which in consequence generate risk. Most of the companies tend to eliminate or minimize risk in their businesses, that is why they regard it as a cost, what in consequence arises the need for innovation. Innovation can be introduced both as a result of deliberate and formal actions or ventures of the research and development departments. in the process of modifying products as well as an informal method of attempts and errors.



The introduction of innovation is usually a highly risky action, especially in the financial sector, because of the threat of easy imitation. This is related to the intangible nature of the service, very high costs related to the introduction of new technologies, growing speed of its changes, the necessity of ensuring high security and competition of the banking sector. Due to all of this factors, it is particularly important to protect know-how, trademarks or patents. Research shows that there is very high risk of failure of introduction of innovation and small percentage of ideas which are chosen to be introduced.

The crucial factor in the process of introducing innovations should be customers needs and expectations. Innovations not only influence particular group of customers, by due to social needs of each person to be understood and accepted among others, it can influence consumption of banking services related to this innovation among other groups. Innovative banking services can become symbols of consumption. The more wealthy becomes the society, the biggest need arises to differentiate itself among people, to achieve the consumption level of groups of higher social hierarchy and imitate the reference groups. During the initial stage of introducing banking service, there is very important role of demonstration which influences the spread of innovation and after some period of time enables general acceptance for the service.

The intangibility of banking services causes that their quality is usually related to image of the bank and attitude and behaviour of bank's employees. Although new distribution channels dynamically appear, the most important decisions still require personal contact. Customers expect more and more financial advices and individual attitude towards them. High competition in banking sector implies that it is not enough for banks to compete only through new types of services. Especially important for them to provide at the same time both elements – innovative technology with high quality contact with bank's employees.



2 Concept of Customer Relationship Management

The concept of Customer Relationship Management has its roots in relationship marketing. The following figure presents the triangle showing differences between those terms.

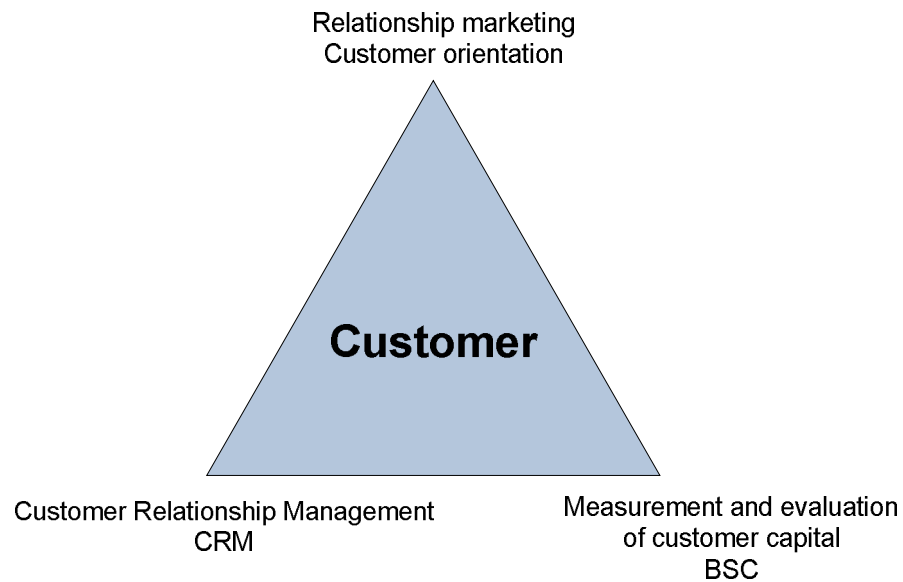
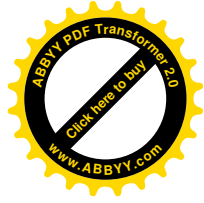


Figure 2.2 Customer Relationship Management

Relationship marketing brought new approach to relations with customers, creating at the same time new market assumptions. CRM is a business strategy focused on maximizing shareholder value through winning, growing, and keeping the right customers. We can distinguish here two important elements. First of all, concentrating on the most important from company's perspective customers and second of all retaining long-term relationship with them. That is why it is essential to collect consequently customers' opinions, complaints and new needs. In this way it is possible to approach a client more individually, and make them feel important for the company, because each company is worth as much as customer values it. Satisfied client will also recommend company's products to their friends. Therefore the main challenges are:

- building long - term partner relations with customers,
- identifying and focusing on the most significant customers,
- acquiring and retaining new customers,

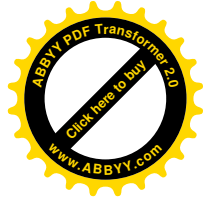


In developing CRM strategies whole organizations should be engaged. It includes adequate approach in terms of sales, marketing and customer support. A truly comprehensive picture of a customer might include information collected by sales partners, suppliers or collaborative service deliverers. When company limits whole its attention only to operational activities, it can decrease communication between business and customer.

Initial CRM implementations should be based on adequate information and perspective about customers and the firm's demand environment. Once implemented, CRM should allow organizations to see beyond the boundaries of the internal enterprise, and collect, analyze, and leverage such insight. It should include following issues:

- understanding markets and customers (gathering market information, selecting target markets),
- ability of dealing with different customers in different ways,
- focusing on one-to-one relations by satisfying needs of individual customers,
- developing an offer (selecting products, positioning, differentiating),
- providing customer care (delivery process, service process, support, loyalty programs).

According to M. Stanusha, the main purpose of the concept from this perspective should be achieving such state, when high \square profitable customers, each time they have a specific need, they would see only one company, that could satisfy it. It is big challenge, however possible thanks to good communication with customer. CRM systems enable any representative of a company to remember who they are talking to, no matter what the transaction might be. It is essential to get to know all the processes used by potential customer to create value. J.Otto said that company which wants to follow rules of CRM concept should use all the means in order to precisely get to know these processes. It should also concentrate on retaining mutual trust between company and customer. The product itself is important, but it is not enough just to produce it, advertise and find recipients. In order that customers keep it in conscience, it is important also to take care of such things as additional service, such as transport, insurance and guarantee. Such activities help to consolidate this relationship and attach customer to the company. CRM enables to differentiate products by adding new dimension, where even mass-produced products can differ with type of relationship which company has with its customers. So there is no point on concentrating on maximization of single transaction, but company should focus on creating



strong and long □ term relationship with customer. The shift to customer-centricity has implications for the entire organization, requiring changes in company's business culture, processes, and supporting systems. However to get full benefits, it is necessary to create interactions which are based on trust between both parties and aim to mutual improvement of this relationship.

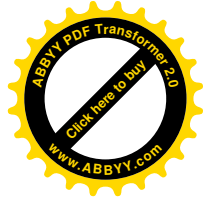
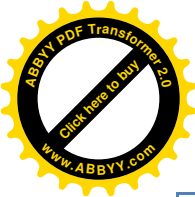
Summing up, CRM as a strategy focuses on building and consolidating a loyal group of regular customers, through constant satisfying of their needs and even going beyond these needs and individual preferences. In order to achieve this goal it is necessary to build strong relationships with those customers based on mutual trust.

3 Benefits of introduction CRM systems

J. Otto divides benefits of introducing CRM systems into two categories: strategic benefits and operational. Following table presents the lists of those benefits.

Table 2.2 Benefits of introducing CRM systems

| Strategic | Operational |
|--|---|
| <ul style="list-style-type: none">▪ Obtaining synergy effects from cooperation between enterprise and the significant customers▪ Increasing profits of the company by limiting investments in non-profitable customers▪ Increasing customers□loyalty by increasing their level of satisfaction▪ Growth of sales | <p>Decrease of operational costs and increase in work efficiency, caused by:</p> <ul style="list-style-type: none">▪ Reduction in time dedicated on administrative purposes by salespeople,▪ Increase of effectiveness of after-sale activities,▪ Reduction in time dedicated to trainings and recruitment,▪ Decrease in amount of complaints▪ Increase of effectiveness of advertisement activities,▪ Decrease in costs of promotion, |

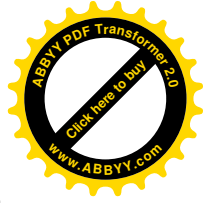


| | |
|--|--|
| | <ul style="list-style-type: none">▪ Saving time of work of employees in promotion department,▪ Possibility of full control budget dedicated for promotion,▪ Estimating effectiveness of particular promotion departments,▪ Control of work of sales departments through estimating state of negotiations with particular customers in whole company,▪ Identifying customers with whom negotiations has stopped in some deadlocks▪ Possibility of evaluating salespeople by:<ul style="list-style-type: none">- Amount of acquired potential customers and its relation to the amount of acquired orders,- Amount of new contracts concerning new and regular customers,- daily, weekly and monthly contacts with customers,- contacts with customers taking into consideration its type (visits, telephones, letters), |
|--|--|

Nowadays more and more companies decide to introduce CRM systems in their companies.

Main factors which facilitate this process and cause its popularity are:

- increase of computing power of computers,
- decreasing costs of buying computers,
- increasing possibilities of gathering information by computers,
- decreasing costs of storing data,
- availability of more and more advanced tools for data analysis, data mining or methods for data visualization,

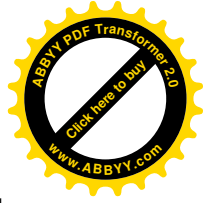


- growth of e-commerce and ways of interacting with customers via internet, due to which the cost of such interactions is much lower than in case of traditional ways,
- increase in awareness of importance of current customers' behavior and importance of customer lifetime value,
- increase of complexity and improvement of marketing approaches, including one-to-one marketing, permission marketing and mass customization,

CRM systems can be used in various types of organizations. However how much company will benefit from such systems depends among other things on level of its customer orientation and characteristics of its branch. In highly competitive sectors CRM systems are especially useful, because due to equal level of technology and similar offer of products the only field to compete between companies operating in such sectors is customer service. We can mention here such sectors as: motor industry, telecommunication, banking, consulting, but also CRM systems become more and more popular in such organizations as universities, health centre and many others. This class of systems is also good for coordinating activities of organization, which is spread geographically in form of networks.

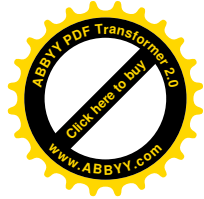
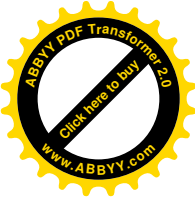
4 Technology in banking

Every day banks have to take many accurate decisions. In order to decrease the risk associated with them, they need to have reliable information. For that purpose they mostly use data warehouses, in which they store all data necessary for conducting business – both those concerning customers' behavior, which enable storing all information in one place and evaluation of customer's risk and those which enable real-time reaction to events on financial markets. For many banks, there exists serious problem of information quality. The main reason for that is the low quality of transactional systems, mainly lack of enough care about data accuracy. However since the size of information is growing, it takes more and more time for analytics to analyze them. That is why there is urgent need for good IT software that could solve those problems. 10 years ago, very popular in banks were easy to introduce, departmental systems. In the moment when the banks started growing, it often turned out that each department has different system for risk management and information about customers was not uniform. And then the banks had to build one central system, which would connect all the separate data warehouses. Nowadays after the



period of centralized solutions, new requirements for IT systems appear, such as open architecture, which arise from the business need of introduction specialized solutions, for example for credits or selling systems, and also the need for integration of systems among given financial group. Main attention in banking sector is put to the systems which enable better usage of customer information and preparing the best offer for them. According to many specialists, the most popular are systems using Business Intelligence, such as CRM systems or decision assistance.

Financial institutions develop customer relationships across a broad spectrum of touchpoints - branches, kiosks, ATMs, internet, PDA, emails, electronic banking, smart cards, call centers, and phones. Additionally CRM systems use various technologies for customer management applications, for example Siebel, Peoplesoft CRM, Oracle CRM, Pivotal, database technologies and architectures such as for example Oracle, Sun, Microsoft. It is very difficult to measure positive impact of technology in banking sector. The main reason for that is the fact that very often it provides intangible benefits, such as customer's satisfaction, for example after introduction of ATMs machines, the expected reduction of branch cost was not accomplished but instead significantly increased the number of customer transactions and customer's satisfaction. The same characteristics had Internet Banking. At the beginning managers thought that it will be a lower-cost delivery channel and a way to increase sales. Studies have now shown, however, that the primary value of offering Internet banking services lies in the increased retention of highly valued customer segments. According to P.A. Dabholkar, when customer is in direct contact with the technology, bank can have greater control, on what they are doing. On the other hand, if there is an absence of direct contact, such as for example in case of telephone banking it is assumed that there is less control perceived by the customer during this transaction. When a consumer freely chooses to use technology as a form of service delivery the impact on their satisfaction is high. Moreover Weatherall claims that consumers have positive perception of technology based services since they believe technology will deliver a faster and more efficient service than that of the employee. However customers put also much attention to efficiency and speed of those services. In some countries with developed systems of electronic banking arose even special sector - electronic private banking (e-private banking), which takes care about providing specialized services, adapted to needs of each customer or has form of electronic wealth management systems.



5 Relations with customers in banking industry

Banks are increasingly developing various marketing strategies in order to develop a competitive advantage that provides customers with superior value compared to competitive offerings. Nowadays there are more and more marketing oriented banks, using IT systems that are focused on individual customers. Very often banking staff dealing with a current account know that the account holder had already a mortgage, credit card and unit trust with the bank. Financial institution using its greatest asset, which is huge knowledge about their customers, can gain their competitive advantage by retaining those customers who represent the highest lifetime value and profitability. Increasing competition, deregulation, and the internet have all contributed to the increase in customer power. There is almost no barrier for customers to switch to another bank, when they find their offer more appealing. Customers' expectations are all the time significantly rising. Customers care now more about the choice than about brand and they expect consistency across multiple channels or "touch points". Therefore retaining customers has become one of the major challenges for financial institutions.

Banks take part in flow of capital between various entities. We can distinguish three types of bank customers: natural persons, business entities and institutions, which either look for beneficial and safe deposit of their money resources or need to borrow some money to finance their consumption or production needs. Natural persons usually have surplus of resources, because they often save them to cover future needs. On the other hand business entities usually have deficit, because they receive profits only after some time and must buy production factors. Additionally they usually are not able to invest only using their own resources and must for that purpose they take out bank loan. However customers among each of the following groups vary significantly, they all have their own specific needs and preferences, they are also aware of the strong position, which they have on the market. Nowadays, bank customers not only expect individual approach, but they also take it for granted. They tend to adapt to new technologies and environmental changes much quicker than banks themselves. Especially in retail banking, if bank does not know how to satisfy its customers, there will be some other one that will be able to do it. For example, when new and modern bank appears on the market, it takes some customers from existing more traditional banks, which can't or don't make the effort to follow the needs of their modern and demanding customers. Nowadays the crucial term in retail banking is the relationship, and not the price or even the quality. Following figure presents how customer's lifecycle changes with time.

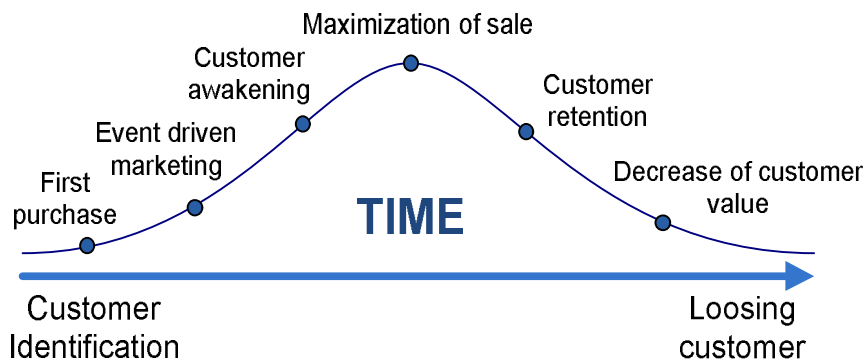
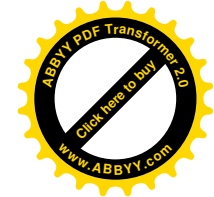
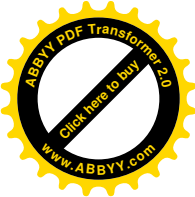


Figure 1.5 Bank customer's life cycle

Banks belong to group of businesses, which possess extended information about their customers. However in many cases collected information is not further effectively used and analyzed. The common problem in many banks is that, this information is spread in many different places and very often stored in various formats, grouped according to their origin, products or organizational structure. Sometimes there is no flow of data between some departments, so there is stored a lot of redundant data. So the main source of problem is not lack of collecting data, but inability to process it. The good knowledge about customers is very crucial and enables - when it is effectively analyzed using business intelligence - to create right proposal in right time for right person using right distribution channel. The main sources of creating information about customers are their profiles, history of operations, contacts and activities, list of transactions, preferences and tastes, complaints, events, or information searched on bank's web page. We can distinguish eight main fields of bank customers' expectations:

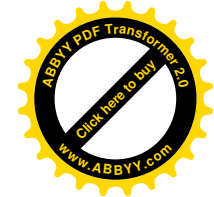
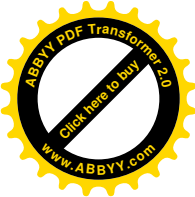
- a) Reliability □ in case of banks reliability is extremely important. Customer expect that the service which they receive will be exactly in accordance with bank's offer
- b) Responsiveness □ they expect that bank employees will be always willing to help them and solve their all doubts. They expect precise and proper answer for their problems.
- c) Appearance □ bank should appear as a professional and trustworthy place in which customer can leave their money safely. The same things concern the image of bank employees.
- d) Accessibility □ they expect that bank and their employees will be available always in the place that they need them.



- e) Competence □ they expect bank employees to have enough professional knowledge which is mandatory to explain them all the technical details and implications of the services which they are going to buy.
- f) Courtesy □ bank's customers expect that employees will be always friendly to them and will behave with respect towards them.
- g) Features □ they expect to get some additional features such as for example ATM card while buying specific bank's service
- h) Clarity □ they expect clear and easy to understand language from bank employees. Customers want communication directed to them to be clear.

Specificity of financial institutions implies that one of the main issues for customers is trust directed toward banks. Bank has to be reliable and stable institution in which customer feel safe to leave their money. The crucial thing in the process of creating bank's customer loyalty is providing high standard service that meets customer expectations. Following steps can be summarized below:

- a) Providing good quality of customer service □ at initial stage, customer stays anonymous for the bank, and can easily move to competition when they decide that their offer is more profitable for them.
- b) Providing professional consultancy □ during the second stage of the relation with bank's customer, the main focus of employees is put on presenting all the financial conditions for the customer of the services offered by the banks also emphasizing all the benefits for customer arising from that service.
- c) Providing account manager □ the main challenge of the account manager is to meet all the individual needs and expectations of their customers, being the intermediary between bank and customer. They should first of all analyze financial condition of the customer, learn about their needs, and keep constant contact with them and advice about the best choices. At this stage customer should notice individual benefits which they gain in this bank.
- d) Partnership □ in this stage the relationship between bank and customer become even wider. Between bank's employees and customer occur personal relations and customer starts to be seen as valuable investment of the bank. In this stage bank offers individual support programs which should meet expectations of the most demanding customers. In

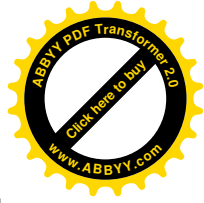


such programs customer receives its own relationship manager, with whom customer has constant contact. The manager is a private financial adviser for customer, at the same manages all financial operations for them and controls customer's financial resources. In this stage customer's loyalty is built basing on visible and specific benefits.

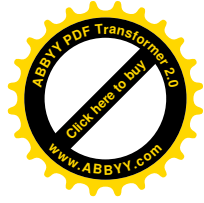
At all of the above stages there is huge role of bank employees which should make positive impression on customer making them feel comfortable and safe trying to meet all their needs. Customer's loyalty directed to a bank, can be expressed their repeatable purchases, or constant use of services, which denotes the big trust for a bank, psychological and emotional involvement. At the same time, it encourages the bank to give the trust back and provide preferential services for those customers. According to some researches made in Great Britain in banking sector, around 50% percentage of customers considers changing their bank. The detailed results are presented in following table.

Table 2.2 Percentage share of bank customers who considered change of their bank

| Name of the bank | Percentage of customers |
|---------------------------------|--------------------------------|
| Barclays | 50,6 |
| Lloyds | 58,7 |
| Midland | 55,8 |
| National Westminster | 53,0 |
| Bank of Scotland | 37,3 |
| Clydsdale Bank | 38,4 |
| Royal Bank of Scotland | 41,2 |
| Average percentage of customers | 51,9 |



In this group of customers, which think about changing their banks probably appear also high valued customers. The results show the big problem with customers' loyalty in banking sector and the importance of improving this relation. Especially essential is the need for learning about the reasons of customers' dissatisfaction. From that perspective, we can consider customer's loyalty like a durable resource. If somebody ignores it, it will have to act in more uncertain and competitive environment, and at the same time, it will have to spend the cost of acquiring new customer, which usually is much higher, than cost of retaining existing one. Additionally, permanent customers are less sensible to price changes and if they are satisfied they tend these products or services recommend it to others. However long relationship with customer does not have to mean bigger profits, banks while creating their marketing strategies must choose factors which are crucial for them such as for example, turnover, length of relationship, share in shopping basket, strength of the relationship, positive opinions which are popularized by customers households or customer's family. In CRM concept, the whole attention is put to processes, which customers use to create value and realize their objectives. In order to get full knowledge about customer, it is necessary to get to know those processes. Very often, there is not enough attention put to customers making purchases on www pages, however Internet due to wide and easy access to much information about competitors' offers is especially dangerous. Moreover there is no distinction in quality of the service, due to lack of personal contact, however in this case very helpful could be online consultations. The interpersonal contacts are crucial in banking services. Research made using detail bank customers showed that limitation of this kind of contact and replacing it with self-service decreased loyalty to a bank, because in this type of services many customers expect personal advices. The common way to reward loyal customers is to give them right to overdraft on their account, preferential credits, simplified procedures or lower prices.

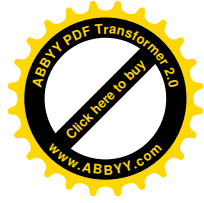


6 Customer Relationship Management as an innovation

CRM can be considered both as an innovation and the result of innovation. CRM systems could appear on the market due to innovation in technology, however on the other hand they also could be considered as an innovation. Unlike other technological innovations, CRM has power to help banks quickly and directly improve customer satisfaction and increase retention of significant customers. Financial institutions started to be interested in CRM systems, due to their need for speed of flow of precise information concerning customers and learning about their customers' individual needs. Nowadays the decreasing loyalty of bank customers, forces banks to put more attention on relationships with them. Banks use CRM system believing that it will help them to identify the point at which customer value balances shareholder value.

Banks almost on each hierarchical level of their structure need to have access to up-to-date, consolidated and accurate image of a client. Especially in conditions of growing amounts of data it is important to be able to share information coming from various channels and afterwards analyze it deeply. If the bank could track customer behaviours, executives can have a better understanding of customer value and predicting their future behaviours. According to Foss, banks use CRM systems for various purposes, such as increase of sales, creating customer-centric culture and organization, improving customer relationships, maximizing customer profitability, aligning efforts and resources behind most valuable customer groups and finally having one central and coherent IT system.

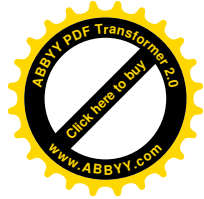
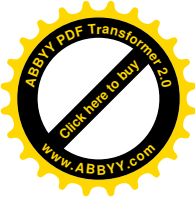
One of the advantages of introduction CRM systems is that it can be in gradually and at each state, the benefits can be measured. Additionally they can be split in modules, so only some specific parts of the CRM can be installed and if there is such need in the future the system could be further extended by other modules. However very often banks are afraid of huge CRM systems and decide only on some parts, for example Call Centre, which at the end does not serve expected purposes. However in case of CRM systems in order to succeed, it is necessary to adjust whole organization to CRM system, and introduce whole solution, what can be done gradually. Every part of CRM system constitutes one consistent whole, otherwise some integration problems might appear.



The most popular functionalities of CRM system in banks concern marketing, communication with customers, customer service, sales, distribution, financial analysis, risk estimation, channel management. All of these features are integrated in one system and together with analytical processes create full and up-to-date image of customer. The main priorities in CRM systems are:

- making the customer service uniform in various distribution channels,
- Real-time customer's information analysis,
- Delivering individualised services, which create added value for customer,
- Building and consolidating customer's loyalty,
- Providing management information, such as service profitability or Customer Lifetime Cycle,

Banks that has introduced CRM system, had to make some difficult changes in their organization in order to become more customer oriented. Beside the pure CRM banks try to adopt other innovative tools related with the core CRM. Some of these solutions are constructed in such a way so that ensured could be also access to the information beside to bank's organization. Other functionalities constitute better content management. Moreover some researchers predict that due to rising demand of financial institutions to improve their relations with customers, many new CRM- related innovations will be invented.



7 Bibliography

1. Dougan S., *Customer Relationship Management Strategies In Financial Services*, London, Business Insights Ltd., 2004
2. W. Scott Frame, Lawrence J. White, *Empirical Studies of Financial Innovation: Lots of Talk, Little Action?*, 2002, article prepared for the conference: □Innovation in Financial Services and Payments□Federal Reserve Bank of Philadelphia
3. Newell F., *Why CRM Doesn't Work: How to Win by Letting Customers Manage the Relationship*, New Jersey, Bloomberg Press, 2003
4. Otto J., *Marketing relacji*, Warszawa, Wydawnictwo C.H. Beck, 2004,